

# The Value of Human Capital: A Micro-Level Approach

By Jack J. Phillips, Ph.D.

In October, we focused on the macro-level view of the value of human capital. August's article explained how value is placed on human capital using logic and intuition—the intangibles. This month, the micro view will be examined, showing how detailed impact studies are conducted on specific human capital projects, initiatives and solutions. This view, which in the past decade has been presented in the form of ROI studies, provides decision-makers with detailed information about the success (or lack of success) of specific initiatives. This analysis also helps drive decisions about future learning and development projects. In addition, these studies can improve ongoing projects. When combined with the macro-level analysis and logic and intuition, ROI impact studies supply the proof of the impact of learning and development. The ROI methodology has evolved into a widely used method to show the impact of human capital programs. The ROI methodology collects six types of data: reaction and planned action, learning, application and implementation, business impact, ROI and intangibles. This process also includes a method to isolate the effects of a particular learning program. The methodology presents a systematic way for planning, collecting data, analyzing data and reporting data. It also includes standards, best practices and implementation guides.

## ROI Progress & Status

The ROI methodology for learning and development had its beginning in the 1970s when it was applied to the development of a return on investment for a cooperative education program at Lockheed-Martin. Since then it has been updated, refined and expanded in all types of situations, applications and sectors.

Perhaps one of the most visible signs of the acceptance of ROI methodology is the proliferation of ROI networks. Founded in 1996, the first global ROI Network was formed by a group of practitioners involved in implementing the ROI process. The purpose of the organization is to promote the science and practice of individual and organizational measurement and accountability. Through Web sites, list serves, newsletters, research grants and conferences, the Network has routinely exchanged information about the ROI process. In 2002, the Network was acquired by the American Society for Training & Development (ASTD). In addition, other networks have been developed for specific countries, regions, states, cities and even companies. Networking has been an excellent way to continue to develop this capability, sharing tools, techniques and technology.

Measuring return on investment is a global issue. Organizations from all over the world are concerned about accountability and are exploring ways to measure the results of programs and solutions. Whether the economy is mature or developing, accountability is still a critical issue. Professional associations in different countries offer workshops, seminars and conferences dedicated to the

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measurement issue. Some associations sponsor individual workshops on ROI. Formal ROI presentations have been made in more than 50 countries with implementation organized and coordinated in at least 35 countries. For example, Skillnet, partially funded by the Irish government and businesses, sponsors workshops on ROI for learning and HR professionals and assists with ROI implementation. Skillnet is taking the lead in coordinating and introducing ROI to organizations in Ireland. In April 2005, Skillnet sponsored an ROI Network Conference that attracted 100 attendees.

There are good reasons why return on investment has gained acceptance. Although the viewpoints and explanations may vary, some things are clear. Learning and development budgets continue to increase annually by organization, industry and country. Many organizations and countries see learning and development as an investment instead of a cost. Consequently, senior managers are willing to invest because they can anticipate a payoff for their investments. As expenditures grow, accountability becomes a more critical issue. A growing budget creates a larger target for internal critics, often prompting the development of an ROI process.

ROI is a familiar term and concept for business managers, particularly those with business administration and management degrees. They apply the ROI process to the purchase of equipment, building a new facility or buying a new company. Consequently, they understand and appreciate ROI and are pleased to see the methodology applied to human capital.

ROI is now receiving increased interest in the executive suite. Top executives watch with frustration as budgets continue to grow without the appropriate accountability measures. For years, learning and development managers convinced top executives that the results of learning and development programs could not be measured, at least as a monetary contribution. Many executives are now aware that they can be and are being measured. Consequently, they are demanding the same accountability from their learning functions. Today, hundreds of organizations routinely develop ROI calculations for human capital programs. Its status has grown significantly, and the rate of implementation has been phenomenal. The number of organizations and individuals involved with the process underscores the magnitude of ROI implementation. With this much evidence of the growing interest, the ROI process is now becoming a standard tool for learning evaluation.

Impact studies have been conducted in every human capital area. As expected, more progress has been made in some areas than in others. For example, productivity improvement and gain-sharing programs have shown tremendous success with the use of ROI. Reward systems and safety programs often show impact with ROI without much difficulty. In the learning and development area, there have been many applications with increasing success. Other areas have not fared so well. For a variety of reasons, ROI progress has not been made in recruiting, compliance, diversity and career management, but the need and interest are still there.

### **ROI Standards & Best Practices**

The ROI methodology has been developed and refined around conservative standards known as “guiding principles,” which provide conservative adjustments, so if there is any error in the study, it is discounted (or removed from the analysis) as a monetary benefit. Also, on the cost side of the equation (when comparing costs to specific benefits), the costs are fully loaded to include all

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expenses—both direct and indirect. These principles serve to increase credibility, but more importantly, obtain buy-in with senior management staff who often view the results of the programs.

### **Barriers to ROI Implementation**

Although progress has been made in the implementation of ROI, significant barriers inhibit implementation. Many of these are realistic, while others are based on false perceptions:

- The ROI process adds cost and time to the evaluation process of programs, although the additional amount is usually not excessive.
- Many learning and development staff members do not understand ROI, nor do they have the basic skills necessary to apply the process within their scope of responsibilities.
- Many of the current learning programs do not have an adequate initial analysis and assessment of need.
- Fear prevents learning and development departments from pursuing ROI—whether it is a fear of failure or the unknown. This fear, often based on unrealistic assumptions and a lack of knowledge of the process, becomes a realistic barrier to many ROI implementations.
- A successful ROI implementation requires planning and a disciplined approach to keep the process on track.
- Many learning and development staff members have false assumptions about the ROI process, which keeps them from attempting ROI.

### **Benefits of ROI Methodology**

Although the benefits of adopting the ROI process may appear to be obvious, several distinct and important benefits can be derived from the implementation of ROI in an organization.

Routine use of the ROI Methodology is the most accurate, credible and widely used process to show the impact of a learning program or project.

Calculating ROI in different areas with different programs and projects will determine which programs contribute the most to the organization, allowing priorities to be established.

The ROI Methodology is a results-based process that focuses on measuring the success of programs, even for those not targeted for an ROI calculation.

Developing ROI information is one of the best ways to earn the respect of the senior management team and the sponsor.

When applied consistently and comprehensively, the ROI Methodology can convince the management group that human capital is an investment, not an expense.

These key benefits, inherent with almost any type of process improvement, make the use of the ROI methodology an attractive challenge for the CLO function.

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